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The Scottish Law Commission's Contract Report 2018

A. INTRODUCTION

The Scottish Law Commission's Review of Contract Law in the light of the Draft Common Frame of Reference (DCFR) came to its conclusion with the publication of a final Report on 29 March 2018 (henceforth "the 2018 Report").¹ The project had been running since the beginning of 2010, and along the way had given rise to the Legal Writings (Counterparts and Delivery) (Scotland) Act 2015 and the Contract (Third Party Rights) (Scotland) Act 2017.² The 2018 Report covers all the other matters upon which the Commission had touched during the progress of the review: in the order in which they are presented in the report itself, formation, interpretation, remedies for breach, and penalty clauses.³ Each subject involved reconsideration of four previous respective Reports made by the Commission in the 1990s which, although not rejected at the time, remained unimplemented by legislation.⁴

Despite this quite wide coverage, the reforms proposed and the draft Bill provisions appended to the 2018 Report are relatively few in number. The major element is a legislative restatement of the law on formation, which includes however the abolition of the postal acceptance rule and the provision of a specific rule on when electronic communications between parties negotiating a contract take their legal effect. Three specific reforms are proposed on remedies for breach, in relation to the principle of mutuality, restitution following rescission, and contributory negligence.⁵ But the suggestion of a general statutory

¹ Report on Review of Contract Law: Formation, Interpretation, Remedies for Breach, and Penalty Clauses (Scot Law Com No 252, 2018).

² See further Report on Formation of Contract: Execution in Counterpart (Scot Law Com No 231, 2013); Report on Third Party Rights (Scot Law Com No 245, 2016).

³ See Discussion Paper No 147 on Interpretation of Contract (2011; henceforth "the 2011 DP"); Discussion Paper No 154 on Formation of Contract (2012); Discussion Paper No 162 on Penalty Clauses (2016; henceforth "the 2016 DP"); Discussion Paper No 163 on Remedies for Breach of Contract (2017; henceforth "the 2017 DP").

⁴ Report on the Formation of Contract: Scottish Law and the United Nations Convention on Contracts for the International Sale of Goods (Scot Law Com No 144, 1993); Report on Interpretation in Private Law (Scot Law Com No 160, 1997); Report on Remedies for Breach of Contract (Scot Law Com No 174, 1999, henceforth "the 1999 Report"); Report on Penalty Clauses (Scot Law Com No 171, 1999).

⁵ Other specific reform possibilities ventilated in the 2017 DP but not taken forward in the light of consultation responses are reform of the rule in *White & Carter Councils v McGregor* 1962 SC (HL) 1; abolition of any rule preventing recovery of certain kinds of non-patrimonial loss caused by breach of contract; reforms of the self-help remedies of retention and rescission and the judicial remedies of specific implement and interdict; making general

restatement on remedies, made in a Discussion Paper published in 2017, is not followed through, in part because of a generally unenthusiastic consultation response and also because the task probably required more time than was available at the end of the review. The formation restatement, on the other hand, had been proposed in a Discussion Paper in 2012 (henceforth “the 2012 DP”) and received much more of a welcome from consultees, while also being the subject of a further consultation as a draft Bill in the summer and autumn of 2017. Finally, in the light of recent Supreme Court rulings on interpretation and penalty clauses,⁶ no recommendations are made for reform in these areas. This note focuses on the reforms actually proposed.

B. FORMATION

(1) A general statutory restatement

The thinking behind the recommendation of a general statutory restatement of the law on formation is founded first on the Commission’s mission to simplify, modernise and improve the law, which includes rendering it more accessible and available. A statutory statement tells people – individuals, small businesses, others lacking legal advice – how to go about the important business of forming contracts. For lawyers, it means no – or less – need to consult textbooks and analyse centuries’ worth of case law to find out what the law is. The statute also provides answers to some problems which are not answered in the present law but seem to need such answers.

(2) Contract formed by sufficient agreement

The draft Bill makes clear that the guiding principle is that contract is a matter of sufficient agreement (in the sense that the essentials of the contract in question are agreed by the parties with enough clarity), showing the parties’ intention to be bound to each other. Offer and acceptance is one way of showing such agreement, and is dealt with in detail in the draft; but this is not the only way to conclude a contract, and it will not become necessary to press difficult facts into the offer-acceptance slots, provided that sufficient agreement between the parties in the sense already mentioned is objectively apparent. Nor need the parties be agreed

consumer remedies of price reduction and cure (repair or replacement); and reforms to clarify the law on gain-based damages and the problem of “transferred loss”

⁶ *Arnold v Britton* [2015] UKSC 36, [2015] AC 1619 (interpretation) and *Cavendish Square Holding BV v Talal El Makdessi and ParkingEye Ltd v Beavis* [2015] UKSC 67, [2016] AC 1172 (penalty clauses).

on all matters under discussion between them: there can be a contract if, again, there is sufficient agreement on the essentials.

(3) Abolition of postal acceptance rule

The draft Bill does include some important reforms alongside its re-statement of the existing law. As already mentioned, they include abolition of the postal acceptance rule, under which a contract is concluded by an offeree posting its acceptance. The 2018 Report finds no good policy reason in modern conditions for privileging postal over other forms of acceptance communicated between remote parties. The rule is commonly excluded by those acting with legal advice. The 2018 Report is concerned that parties acting without legal advice may be taken by surprise by some of the rule's effects (e.g. that an acceptance posted within an offer's time limit is effective even if it arrives with the offeror after the deadline has expired; or, indeed, possibly if it never arrives at all).

(4) Communications effective upon reaching addressee

The basic position set out in the draft Bill is that all communications between parties negotiating a contract take effect upon "reaching" their intended addressee. This is objectively tested: in the words of the draft Bill, "when it is made available to the person in such circumstances as make it reasonable to expect the person to be able to obtain access to it without undue delay." So it is not a matter of when the addressee subjectively knows that there has been a communication and what its content is. The draft Bill also clarifies when electronic communications take their intended legal effect, whether as offers, acceptances, withdrawals, or revocations of previous communications. The proposed rule would be that "reaching" occurred when the communication is reasonably available to the addressee, with all relevant circumstances to be taken into account in assessing reasonableness.

The proposed rule has implications for "out of office" email messages. Take the simple case of an emailed acceptance of a preceding offer, to which the sender of the acceptance receives an automatically generated "out of office" reply. Such a reply will need to be well-framed to say fairly precisely for how long the recipient expects to be out of office in order to prevent the emailed acceptance having the legal effect of concluding the contract, if not immediately, then fairly soon after transmission when it is "reasonably available". It will not do for the automatic reply to say something like "I expect to have only intermittent access to my email during this absence"; such access could take place as soon as the acceptance email arrives, after all, and the acceptance must be treated as "reasonably

available” at that point. Equally, an out of office email surprising the sender of the acceptance by announcing that the addressee is on holiday for the next two weeks without providing an alternative contact authorised to do business on that party’s behalf, or instead of that party, would be unreasonable, and the acceptance should be treated as available to the recipient.

(5) Change of circumstances before contract concluded

The 2018 Report also makes recommendations on the lapsing of offers and acceptances by reason of change in the parties’ circumstances before any contract is concluded. The recommendation in general is that an offer, or an acceptance that has not yet concluded a contract (for example because it has not yet reached the offeror), should lapse upon a fundamental change in either party’s circumstances. The draft Bill has specific provisions saying that death or loss of capacity is such a fundamental change of circumstances, and that insolvency is not. Obviously the latter can apply to corporate entities, but not the former. It will be a rare case where a company having made an offer or sent an acceptance ceases to exist before the contract is concluded, but it is not impossible, as pointed out during the 2017 consultation on the draft Bill.⁷ That case will however fall to be considered under the general rule on fundamental change of circumstances and if necessary, it will be for a court to decide whether the company ceasing to exist is such change of circumstance.

(6) The battle of the forms

There is no specific recommendation on the problem of the “battle of the forms”, although the 2012 DP canvassed various specific solutions to the problem arising where negotiating parties exchange their incompatible standard forms of contract and proceed to performance without sorting out the differences between them. The consultation showed no consensus on any of these solutions, with it being apparent that the existing uncertainty would be replaced, not by certainty, but with new uncertainty. In the end, the 2018 Report suggests that the general principle of agreement provides the best possible solution to the problem. The court should look to see if it can identify sufficient agreement on the essentials of the particular contract along with an intention to be bound in how the parties have actually behaved, and base a conclusion of contract (or not) on these considerations. There are examples of such an approach in the case law.⁸ While under the draft Bill it will remain possible, as at present, to

⁷ 2018 Report, para 6.23.

⁸ Citations and discussion can be found at 2018 Report, paras 4.39-4.42.

use offer-acceptance doctrine to analyse the exchange of forms, the 2018 Report highlights the arbitrariness of the results that tend to follow from such an approach, and for that reason prefers the “agreement” approach as more likely to produce a substantively fair or commercially justifiable decision.

(7) A system of default rules

The formation rules in the draft Bill are explicitly “default” in nature, and parties will be free to set up their own alternatives if they wish to do so. That could be by pre-contractual agreement between them; or one of the parties might make a declaration in advance of what is needed to bind it in contract (e.g. under the present law, say that a posted acceptance will conclude a contract only upon receipt); or the parties may make an agreement that would be a contract under the Bill but for its inclusion of a term saying that there will be no contract until the parties have executed the agreement in formal writing. A good example is provided by the Amazon website: when the customer completes an order (which is an offer), the website sends an email acknowledging receipt of the order but saying that there is no contract until the ordered goods are despatched. That way Amazon avoids liability if there is no stock available to meet the customer’s order. But it also creates in advance of any specific contract a rule as to what constitutes its acceptance which gets around the Bill’s rule on “reaching”.⁹

C. REMEDIES FOR BREACH

(1) Mutuality

The first proposed reform on remedies relates to the doctrine of mutuality of contract in so far as it seems to say that a party in breach of contract is thereby disabled from claiming any performance due to it by the other party. In its 1999 Report on the matter the Commission thought that this view had been shown not to be right by a dictum of Lord Jauncey in a House of Lords case.¹⁰ That this was an optimistic assessment has since been demonstrated by inconsistent decisions from the courts and continuing confusion in practice.¹¹ The 2018 Report therefore suggests that the law could be made clearer by a legislative statement that a

⁹ The customer is initially licensed to use the website by accessing it or by opening an account; the licence also contains the terms about how contracts for the supply of particular items will be concluded. Amazon further does not take payment for items ordered until after their despatch.

¹⁰ 1999 Report, paras 7.8-7.13 (relying on *Bank of East Asia v Scottish Enterprise* 1997 SLT 1213 at 1216L per Lord Jauncey).

¹¹ See 2018 Report, paras 10.4-10.7.

party in breach of contract (A) can nevertheless claim performance from the other party (B) unless (1) the performance in question is being lawfully retained or withheld by B (that is, B is exercising the remedy of retention or withholding performance in respect of A's breach); or (2) B's performance fell due only after lawful termination of the contract by B (that is, B has rescinded the contract for A's material breach). Thus, for example, in the classic case of *Graham v United Turkey Red*, the agent (A) would be able to recover commission on his post-breach sales up to the point where his principal (B) terminated the agency contract for that breach.¹² The reform is conceivably one that could be effected by the courts; but, as always with this possibility, the questions are how long that might take, and what advice clients might meantime be given on the subject.

(2) Restitution after rescission for material breach

The second recommendation for reform in the 2018 Report aims to develop the law by filling a gap or dealing with a problem where the common law is incomplete. The subject is restitution after rescission (or termination) of a contract for a party's material breach. There has been much writing and some cases on this matter over the last quarter century, but no consensus has emerged on how it should be treated by the law. In particular there have been varying views on whether it is a matter for the law of unjustified enrichment or is rather an aspect of contract law akin in some (but by no means all) ways to the operation of *restitutio in integrum* with regard to voidable contracts. The DCFR on the other hand contains a detailed scheme for restitution upon termination of contract for non-performance, whether "excused" (i.e. frustration) or "un-excused" (i.e. breach). In essence the 2018 Report and draft Bill present a rewritten version of the DCFR provisions, applying however only in cases of rescission for material breach where the termination leaves a party (whether or not the one in breach) with the benefit of an unreciprocated performance by the other party. But a footnote to the 2018 Report draws attention to the possibility that the scheme might also provide a more satisfactory solution to the problem of how to deal with performances rendered but not reciprocated after, not only termination for breach, but also frustration (where at the moment the law of unjustified enrichment applies¹³). Note is also taken of Sonja

¹² *Graham v United Turkey Red* 1922 SC 533.

¹³ See *Cantiere San Rocco SA v Clyde Shipbuilding & Engineering Co Ltd* 1923 SC (HL) 105.

Meier's 2017 Wilson Lecture, which suggested that something like the scheme might also be applied to the unwinding of performances rendered under void and voidable contracts.¹⁴

(3) Contributory fault

The 2018 Report follows its 1999 predecessor in recommending the introduction of a general defence in damages claims where the pursuer's conduct has contributed to its own loss. The effect of this will be to reduce the amount of damages to be awarded to the pursuer. The chosen method of reform is however different from that proposed in the 1999 Report. It proceeds, not by way of a free-standing provision, but by amendment to the Scotland-only provisions of the Law Reform (Contributory Negligence) Act 1945, the wording of which has been generally understood to mean that the defence of contributory negligence is only available in breach of contract cases where the defending contract-breaker's liability in contract is the same as its negligence liability in delict, independently of the existence of any contract. It thus appears that under the present law a contributory negligence defence is available to contract-breakers if their contractual obligation is concurrent with a delictual obligation, or an obligation that would give rise to a breach of statutory duty, regardless of whether the pursuer chooses to frame its action solely in terms of breach of contract.¹⁵ The 1999 Report remarked, in words approved by its 2018 successor, that "it is not justifiable to draw a distinction between contracts involving the exercise of care and skill and other contracts";¹⁶ and the 2018 Report also approvingly cites an academic commentator's observation that "it brings the law into disrepute if [defenders] are left to argue that [pursuers] were negligent, whilst [the latter] deny this."¹⁷

The proposed solution is to make the definition of "fault" in section 5 of the 1945 Act subject to a new provision, with the effect of extending the definition to include "breach of contract". As the 2018 Report remarks,

This approach has the benefit of leaving in place all the other relevant jurisprudence under the 1945 Act as well as making clear the intent not to open up a completely new

¹⁴ S Meier, "Unwinding Failed Contracts: New European Developments", (2017) 21 EdinLR 1.

¹⁵ The leading case is thought to be *Forsikringsaktieselskapet Vesta v Butcher* [1988] 3 WLR 565 (CA). See further 2018 Report paras 10.35 on the Scottish position. The 2018 Report also draws attention at para 10.34 to the argument that the *Vesta* case has been impliedly overruled by subsequent authorities.

¹⁶ 1999 Report, para 4.11; 2018 Report, para 10.36.

¹⁷ R Stevens, "Should Contributory Fault be Analogue or Digital?" in A Dyson, J Goudkamp and F Wilmot-Smith (eds), *Defences in Tort* (2015), p 247; 2018 Report, para 10.46.

kind of defence for breach of contract separate and distinct from contributory negligence as it has been previously understood.¹⁸

In particular, this means that the amount by which the damages are to be reduced is not necessarily proportionate to the relative causal potency of the respective parties' conduct; it rather continues to be a question of what the court considers "just and equitable", having regard to the blameworthiness, foolishness or unreasonableness of the pursuer's conduct.

(4) Default rules

In line with the Commission's general policy in its review of contract law, the draft Bill makes both the new rules on mutuality and on restitution after rescission subject to the parties' freedom to provide otherwise in their contract. Matters are however a little more complex with the rule on contributory fault. To start with, it is not clear whether it is possible to contract out of the application of the 1945 Act. The proviso to section 1 of the 1945 Act may however indicate that it is:

Provided that—(a) this subsection shall not operate to defeat any defence arising under a contract; (b) where any contract or enactment providing for the limitation of liability is applicable to the claim, the amount of damages recoverable by the claimant by virtue of this subsection shall not exceed the maximum limit so applicable.

The 2018 Report also notes that Glanville Williams (who made the deepest scholarly study of contributory negligence so far published, but said nothing directly on the point under the 1945 Act) did say of the common law position in England & Wales before the Act that "[i]t need hardly be doubted that the defence of contributory negligence cannot be set up if it was the intention of the contract to exclude it."¹⁹ The Commission avoids any doubts in relation to its new rule by recommending that the new contributory fault rule for breach of contract should be subject to contrary provision in parties' contracts.

D. CONCLUSIONS

Available space precludes any detailed critique of the 2018 Report summarised above, even if indeed the present writer is in any way suitable for the task, having led the Commission's review of contract law throughout its course. While he remains committed in principle to the

¹⁸ 2018 Report, para 10.51.

¹⁹ 2018 Report para 10.55, quoting Glanville Williams, *Joint Torts and Contributory Negligence: A Study of Concurrent Fault in Great Britain, Ireland and the Common-Law Dominions* (1951), at 222.

view that the best way forward for Scots contract law would be by way of statutory restatement,²⁰ the complexities of the law reform process have also to be recognised and accepted. In particular, while legislation must be the primary tool in that process, it is possible for the courts (or at least the Supreme Court, as shown for example by *Arnold v Britton* and *Cavendish Square Holding BV v Talal El Makdessi and ParkingEye Ltd v Beavis*) to have agency in this as well.²¹ Judicial and practitioner use of the critical analyses of the law in the 2018 Report where, however, no recommendation is made for *legislative* reform will be as revealing in this regard as any decision that the Scottish Government may make as to parliamentary implementation of the specific proposals made by the Commission.

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²⁰ H L MacQueen, “Quo Vadis?”, 2017 JR 9-19.

²¹ That lower courts have a law reform role to play too was acknowledged by Lord Justice Clerk Carloway (now the Lord President) in a speech made in April 2015: “To ‘Mend the Lawes, That Neids Mendement’: A Scottish Perspective on Lawyers as Law Reformers”, accessible at https://www.scotlawcom.gov.uk/files/6614/3030/0488/CALRAs_Biennial_Conference_-_Lord_Justice_Clerk_-_11_April_2015.pdf.